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Presentation to the
Legislative Assembly of Ontario
Standing Committee on General Government

COMMENTS ON THE ONTARIO
CONSULTATION PAPER ON RENT DECONTROL

22 August 1996

Comments on proposals contained in
Tenant Protection Legislation: New Directions for Discussion
Government of Ontario, Ministry of Municipal Affairs and Housing, 1996.

What is the problem? Rental supply.

The introduction to the consultation paper states that the “Harris government knows there is trouble in the Ontario rental housing market.” This “trouble” is due to the fact that “the private sector has no interest in investing in rental accommodation.” I do not know of any informed observer who could disagree with this starting observation.

What happened to market demand for new rental supply?

Markets consist of *supply* and *demand*. If we agree there is no private sector supply, what happened to private sector demand? Is there no demand for rental housing in Ontario? If there is market demand for a good or service, there will logically be market supply. In order for a good or service to be supplied on a market basis the ‘demand’ needs to be *effective* market demand. Any ‘business plan’ includes an analysis of the number, type and price sensitivity of potential customers. If there are not enough customers able to afford a particular product, there can be no long-term viable business supplying such a product.

The ‘income gap’ between home owners and renters: 80% in Toronto.

There is very little supply of new rental units in Ontario because there are not enough ‘paying customers’ for newly built rental units. There is simply very little *effective market demand* for new unsubsidized private sector apartments. Very few tenants can afford the rents new construction require. Many tenants, perhaps a vast majority throughout the province, have difficulty paying rent on their existing older, lower rent, apartment units. About one-third of all tenants in Ontario are receiving social assistance. The median income of tenant households is about half that of owners. Using the Toronto CMA as an example, the real (1991 constant dollars) income of tenant households has declined by 8% between 1971 and 1991 while that of owners has increased by 20%. In 1991 tenant households in the Toronto CMA had a median income of \$33,500 while owners had an income of \$64,000 – a gap of \$30,500. [Attached to this paper (Appendix #1) is a three page review of recent trends in housing demand and supply in greater Toronto. About half of all renter households in Ontario live in the Toronto CMA]

Ontario has more “social need” than “effective market demand.”

Very few tenant households in Ontario can pay the rents new construction require. There is thus tremendous *social need* for rental housing but very little market demand. Markets cannot and will not respond to social need. There is a small high end ‘niche’ market for luxury rental (though condos tend to meet this segment of demand). Other than this small niche, investment in new rental housing is not economically viable. Rent controls are not responsible for the serious problems with rental supply. The macro-economic conditions which emerged in the early 1970s are responsible.

Which came first: rental market failure or rent controls?

Ontario’s Rent controls were introduced in July 1975. The government’s consultation paper contains an appendix with some helpful graphs explaining why a Conservative government in 1975 had no choice but to respond with rent regulations.

- Vacancy rates fell dramatically between 1971 and 1974, from about 3.5% to close to 1%.
- Private rental starts fell from a peak of about 40,000 per year in 1972 to a few thousand in 1975.
- Ontario’s consumer price index climbed dramatically throughout the 1970s peaking at close to 12% in 1981 with interest rates reaching 21% in August 1981.

These negative trends began for both tenants and investors *before* rent controls. The early 1970s saw the beginning of ‘stagflation.’ The old economic rules for rental supply, as for many key sectors of the economy, were rapidly changed. Mortgage interest rates were not only at historic highs but were deregulated and unpredictable. The baby boomers were entering the ownership market for the first time, pushing up housing and land prices. Condominiums were introduced in the early 1970s for the first time, allowing higher income tenants to own their apartments (thus decreasing market demand for new rental units).

Market failure.

When these negative macro-economic conditions are combined with the growing lack of effective market demand – the very low and falling median income of renter households in the province – market failure is the result. The ‘demand’ for rental housing is not effective market demand. There can be and will be no supply response under these conditions. Rent regulations are a *response* to market failure. Ending rent controls will have no positive impact on the supply problem – the lack of effective market demand. Macro-economic factors, not a set of regulations, have caused the rental supply problem.

Insupportable claims about the negative impact of rent controls.

There simply is no reliable evidence that rent controls *produce* the range of negative impacts commonly attributed to them. Rent controls in Ontario are a response to a problem, not the cause of the problem. Rent controls are introduced grudgingly by governments in response to severe market realities which allow owners so inclined to take advantage of their market situation (e.g., by rent gouging) in a market where the supply and demand mechanism no longer functions. The impacts of rent control must be assessed on a case by case basis in each jurisdiction, taking into account local market conditions and the specific regulations of the system under examination, including the system's loopholes and inconsistencies.

Building Maintenance Discouraged.

We are told by the Ontario government that the "current system does not ... create any incentives for landlords to put money into maintenance...." On what research is this assertion based? With or without rent controls landlords, like individual home owners, make decisions on maintenance based on the expected market resale value of their property. One of the more dynamic segments of Ontario's real estate market is the buying and selling of existing rental buildings. Existing units are a great investment option for some. [See for example: "Investors go apartment hunting," *Globe and Mail*, July 2, 1996; "Buyers snapping up Metro apartments," *Toronto Star*, March 10, 1996.] There is also a great deal of evidence pointing out that a rent control system like Ontario's with set annual increases and related provisions does not have the theoretically assumed negative impact on maintenance.

- *"Most evidence suggests that modern rent controls have little or no impact on the amount of investment in rental housing. Such a finding is primarily because of the non-restrictive nature of most current rent control ordinances ... that allow for annual rent adjustments to cover increases in operating costs."* – R.P. Appelbaum and J.I. Gilderbloom, "The Redistributive Impact of Modern Rent Control," *Environment and Planning A*, Vol 22, 1990.
- *"A major conclusion of this paper which has relevance for housing policy is that particular features of rent control regulations significantly affect the impact that rent control will have on housing maintenance and the quality of dwellings."* – N.K. Kutty, "The Impact of Rent Control on Housing Maintenance: A Dynamic Analysis Incorporating European and North American Rent Regulations," *Housing Studies*, Vol 11(1), 1996.

New Construction Discouraged.

The government also claims that rent decontrol upon vacancy and the weakening or abolition of other forms of tenant protections "removes barriers to new investment." This is illogical. The existing stock of rental units with their existing tenants represent the past in terms of rental supply. How will forcing existing tenants into paying higher rents for the same old units lead to new investment? How many existing owners of rental buildings actually built their buildings and how many are currently residential developers? If there was *effective market demand* for new rental buildings, they would be built. If there is mainly or only social need, the market will not respond. The government is using an 'ideal

type' theoretical argument assuming 'ideal market dynamics.' The world is not an ideal place and what is called 'nonideal theory' is the proper starting point for policy analysis.

- "By *nonideal theory* I mean a normative theory that takes into account the uncertainties and complexities of actual practice; that descends from the realm of neat generality to the realm of messy particulars." – M.J. Radin, "Residential Rent Control," *Philosophy and Public Affairs*, Vol. 15(4), 1986.

Reviving private rental investment – the failed B.C. experiment.

In 1983 when the British Columbia government introduced measures similar to those now being proposed for Ontario the minister responsible for rent control asserted that "these deregulatory measures will ultimately result in new real estate development, more jobs and a continuing healthy availability of rental accommodation." A dozen years later "British Columbia is home to the lowest vacancy rates and some of the highest rents in Canada." [*Rental Housing Trends in British Columbia*, BC Ministry of Housing, 1995.] There has been no supply response in B.C. Rents went up and during the late 1980s prosperity a great deal of rental stock was either demolished or converted to condos. [See my attached July 2, 1996 memo, Appendix #2, for a summary of the B.C. experience with rent decontrol.]

There is no doubt that rent controls can distort and inhibit the functioning of *normal* market dynamics. The B.C. Social Credit government used this argument in the early 1980s. They did everything they were advised to do according to the assumptions of conventional economic theories. The rental supply experiment failed because there were no normal market dynamics to distort or inhibit. The starting assumption for the policy change was simply wrong. The problem with supply was and remains the lack of effective market demand in British Columbia – as it is in Ontario. [See Appendix #3 for a summary of the impact of removing rent controls on rental supply in Vancouver.]

The rationale for rent controls: Regulatory protection due to market failure.

Vacancy rates of at least 3 or 4 percent provide the market protection tenants require. There are plenty of opportunities to move and landlords worry about losing tenants and having vacant units. One vacant unit for one year (at \$800/month) costs \$9,600 per year. A portfolio of 500 units with 4 percent vacancy during a year (20 units) costs \$192,000 in lost rent. The market provides a severe fine for landlords who are unable to attract and keep tenants.

When there is inadequate market demand and thus little new supply – market failure – vacancy rates remain low and tenants require adequate regulations to provide some degree of balance in the landlord/tenant relationship. Given the rental market failure which emerged in the early 1970s in Ontario's larger metropolitan areas there are four rationales for rent regulations in this province:

1. Security of tenure (protection from economic evictions);
2. Maintenance of the affordability of the existing rental stock;
3. Prevention of a regressive income redistribution; and
4. Mediation of conflicts relating to rental tenure.

[For a discussion of these see: K. Hanly, "The Ethics of Rent Control," *Journal of Business Ethics*, Vol. 10, 1991; and J.D. Hulchanski, *Market Imperfections and the Role of Rent Regulations in the Residential Rental Market*, Ontario Commission of Inquiry into Residential Tenancies, Research Study No. 6, 1984.]

No system of rent regulations is perfect. Any system has its complexities and inefficiencies. We do not live in an ideal world. Change in the existing system must be based on an identification of what is specifically wrong and on what specific measure will likely address the problem. The government's proposals do neither.

The likely impact of the government's proposals.

On security of tenure.

Rent decontrol upon vacancy provides an economic incentive for landlords to use whatever means necessary to get existing tenants to move. The government's consultation paper is based on the assumption that landlords will act in an economically irrational fashion. It is economically rational for owners of rental buildings to maximize the rent levels and for some to consider a different use for their buildings and land (i.e., to consider evicting all tenants so as to obtain the 'highest and best use' for their investment through conversion or demolition). The government's proposals eliminate many of the current security of tenure protections *and* provide owners with an economic incentive to force tenants to move.

On maintenance of the affordability of the existing rental stock.

The end of the housing stock protection provided by the *Rental Housing Protection Act* means that vacancy rates will be much lower due to the loss of units to demolition and to the ownership sector (tenure conversion). Tenants will pay more but most will not receive more and there will be fewer apartments available. Landlords who currently maintain their buildings properly and treat tenants fairly will likely continue to do so (but at higher rents) and landlords who do not maintain their buildings will likely continue their current practices (but also at higher rents). The government's proposals do not protect the existing rental stock from arbitrary and unfair rent increases. The proposals do not effectively encourage maintenance since demolition will become an option. By allowing demolition the government is providing an economic incentive for some owners to cease maintaining their buildings.

On prevention of a regressive income redistribution.

The primary landlord/tenant issue is the amount of the monthly rent. The government's proposals not only allow but encourage a massive transfer of money from tenants to those

who are lucky enough to own rental property in the province. Let us assume conservatively that only *one-third* of Ontario's 1.3 million tenant households (433,300) will pay higher rents due to rent decontrol upon vacancy over the coming *three years* and that the monthly increase is only \$100. This is a redistribution of \$520 million from tenants to rental property owners. What will tenants receive for this money? How will paying additional money to existing owners result in an end to market failure (the assumed ideal of supply and demand in equilibrium in a purely private rental market)?

On mediation of conflicts relating to rental tenure

Macro-economic conditions, at the regional, national and global levels, are not likely to improve the financial situation of lower income households in Ontario. Many renters will never be able to become home owners and many will not be able to afford higher rents. The government's proposals will unleash some of the most bitter and mean clashes between landlords and tenants. The government is at the same time eliminating a system of mediating these conflicts without even proposing a new one: "The ministry has not yet developed a proposal for the new dispute resolution system."

The government's "trickle down" assumption.

A part of the assumed 'ideal' market outcome resulting from the removal of tenant protection regulations is that some investors will build at least some units and that even though these will be at the higher end of the market other units will 'trickle down' to lower income tenants. It is assumed that existing higher income tenants will leave their rent controlled units and move into these newer and potentially nicer units with their much higher rents, allowing others to move into their previous older and presumably lower quality and lower rent units. This process assumes economically irrational behaviour on the part of higher income tenants who could easily buy a modest condo and, in any case, are being provided with a rent controlled unit as long as they do not move. When they do move, the rent on their apartment can be raised. Furthermore, the end of the *Rental Housing Protection Act* means that many of the vacated units will be demolished or converted. Ontario's larger cities have a twenty year history of residential 'up filtering' – gentrification. The end of the down filtering chain is the slum. A visit to most any U.S. city demonstrates the results of residential down filtering. [See Appendix #4 for a brief overview of the concept of 'filtering' in housing markets.]

Assertions vs. Evidence

I shall suggest that the real purpose of rent control is to make it possible for existing tenants to stay where they are, with roughly the same proportion of their income going to rent as they have become used to, and that in light of this purpose rent control might be justified more readily in some particular circumstances or contexts than in others. Thus the analysis I suggest is an

all-things-considered weighting of each situation in light of moral factors relevant to the particular situation.

– M.J. Radin, “Residential Rent Control,” *Philosophy & Public Affairs*, 15(4), 1986.

Throughout the consultation paper there are numerous assertions that certain rules or regulations or legal protections do not work, are harmful, are inefficient, provide barriers, and so forth.

- Where is the evidence for any of these assertions?
- Where is the analysis that the proposed new regulations will be better than the existing ones?

The assertions are followed by proposals that benefit owners of existing rental stock, mainly the large corporate owners. There is no conceivable way that tenants will be any better off. There will be no significant supply of new rental units because the problem – the lack of effective market demand – is not even recognized. The number of tenants forced out of housing altogether will continue to grow as a result of these proposals. There is already a process of “dehousing” taking place in Ontario’s cities. Growing numbers of individuals and families who cannot afford to pay rent any longer find themselves doubling up with others for a while and/or finding themselves in rooming houses, shelters on the street. These proposals will harm the most vulnerable tenant households in the province.

The certain impacts of the government’s proposals include:

- ***rent gouging*** – the transfer of a huge amount of money from tenants to owners with very little if any benefit in exchange;
- ***‘dehousing’*** – the harassment of some tenants by some landlords so as to obtain a vacant rent-decontrolled unit;
- ***demolition and conversion of rental stock*** – even tighter vacancy rates due to the loss of rental stock once the *Rental Housing Protection Act* is abolished; and
- ***glutting the condo market*** – for a few years at least, there will be construction job losses, a potential decline or stagnation of property values for condo owners, and a potential loss of new municipal tax base as existing rental units are converted to condominiums (i.e., units which can be sold for less than the cost of new construction).

To arrive at these conclusions we need simply examine the patterns of *rational economic behaviour* which will result under the proposed new regulatory environment.

In summary, rent controls and the related tenant and rental stock protections that currently exist are a *response* to the problem of inadequate supply, they are not the *cause* of the problem.

This committee should recommend that these proposals be scraped and that new proposals for rental housing supply be brought forward based on a recognition of the problem of the lack of effective market demand among Ontario’s tenant population.

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Copy of July 2, 1996 memo to Housing Minister Al Leach

(with four page extract from a study of the 1983 BC rent decontrol policy)

#3. The Impact of Removing Rent Controls in B.C., 1983

From *Rental Housing Trends in the City of Vancouver*, UBC Centre for Human Settlements, Research Bulletin, April 1989.

#4. The Filtering Process

From *Market Imperfections and the Role of Rent Regulations*

Commission of Inquiry into Residential Tenancies, Research Study No. 6, 1984.

J.D. Hulchanski, University of Toronto
22 August 1996 Presentation to Ontario Legislature,
Standing Committee on General Government

APPENDIX #1

HOUSING PATTERNS AND PROSPECTS IN METRO TORONTO

**Copy of June 12, 1996 speaking notes to
a Committee of Metro Toronto Council**

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Speaking Notes

Metro Toronto Planning and Transportation Committee, 12 June 1996

Subject

Housing Patterns and Prospects in Metro: Greater Toronto's Inner Half
Report by Metro Planning, June 1996

It takes time for our thinking and our practices (policies and programs) to catch-up with changed realities. I consider *Housing Patterns and Prospects in Metro* to be a very important and highly competent study of the changed realities – the key trends and issues – affecting Metro and the GTA. It is our job to reflect on this material and design appropriate courses of action. I will focus my comments on rental housing demand and supply.

1. Rental Housing Demand

We need to be careful when we use the term *demand*. When developers and economists use the term they are referring to *effective market demand*, that is, people who are able and willing to buy or rent a particular product. In housing research the term tends to include these people as well as people who *need* housing. People who need housing but do not have enough money to generate effective market demand generate, instead, *social need*. The market does not respond to social need.

Virtually the entire housing study documents the nature and extent of the problem: an increasing percentage of Metro residents cannot generate effective market demand for housing. One of the clearest summaries of why this is the case is provided in the table below. The gap between the household income of owners and renters has increased dramatically. Homeowners in the Toronto area have incomes almost double that of renters. The median income of owners increased in real terms since 1971 (up 20%) while renters' incomes have declined (down 8%). The 1996 census will likely

Median Household Income, Toronto CMA, Constant 1991 Dollars

	1971	1991	Change	
owner	\$53,500	\$64,000	+ \$10,500	+ 20%
renter	\$36,500	\$33,500	– \$3,000	– 8%
GAP	\$17,000	\$30,500	+ \$13,500	+ 80%

based on Census data in Table 2.3.17 in Appendix A, p.18.

show that the situation is much worse now than in 1991. These figures, furthermore, are for the entire region. The lowest income renters are concentrated within Metro.

The report points out that polarization is taking place among the GTA's households in terms of income, tenure and location. These trends include: households able to pay for housing are leaving Metro (young family owners); households who are staying tend to be seniors, lifelong renters and non-family households (now 50% of households in Metro are renters); and new residents, migrants and immigrants, tend to be renters and tend to settle in Metro.

2. Rental Housing Supply

"There is little prospect for new rental apartment construction (irrespective of rent control abolition) in view of construction costs versus rents which tenants can afford to pay." (page i)

It is the lack of *effective market demand* that explains why rental housing cannot be built by the private sector. Many tenants have difficulty paying *existing* market rents and very few can afford the much higher rents required to make new construction profitable. Recent and likely future trends mean that there is a great deal of *social need* rather than effective demand for rental housing in Metro.

It is not surprising, therefore, that there were only 800 private rental starts in Metro between 1991 and 1995. During the same period 12,600 social housing units were built. Provincial and federal housing policy now means that there will be very few if any social housing starts in the future. Yet, as but one indicator of the scale of housing need in Metro, there are 34,000 households on the MTHA waiting list – households that have passed a very strict needs test qualifying them for rent-geared-to-income housing. The small number of higher income renters are having their demand met by the many investor-owned condo's and houses that are currently available for rent.

We need to recognize that the *supply and demand market mechanism* does not and cannot work in Metro's rental housing sector. There is too much social need and too little effective market demand. Given the income trends among owners and renters identified above, in combination with current provincial and federal housing and income support policies, this situation will become much worse into the foreseeable future.

This means that there is *market failure* in the rental supply mechanism. It is not simply a problem of government imposed impediments (e.g., regulations, rent controls, etc.). What some call market impediments are simply forms of consumer protection given that market failure has occurred. The existing rental stock needs to be protected from demolition and conversion, thus we have rental housing protection legislation. Households who have no choice but to be renters need to be protected from those who would take advantage of the fact that there is little new supply, thus we have rent controls.

In British Columbia rent controls were abolished in 1983, so as to 'allow the market to function normally.' There has not been a rental supply response from the private sector. Nor can there be. The gap between the incomes of owners and renters in BC is about 60%. As of 1995, twelve years after rent controls were abolished, "British Columbia is home to the lowest vacancy rates and some of the highest rents in Canada." (*Rental Housing Trends in British Columbia*, BC Ministry of Housing, 1995.)

3. The Shelter Allowance Debate

In an ideal world there would be less income inequality and the gap between the income of owners and renters would be much smaller. Then there would likely be more effective market demand for housing and less social need.

A shelter allowance program, if it were to address the lack of adequate income among many households, would be an expensive new entitlement program. The reason the federal government rejected shelter allowances after a great deal of careful study in the mid-1980s is very simple: the cost of the program. In an ideal world we would spend the money to achieve a more just society. In an ideal world we would not cut income support for the poor and increase the income of others through tax breaks.

The Example of OHC

In a non-ideal world we need to figure out a range of practical and feasible options that best address at least some of the realities we face. An example of one such option was the establishment of the Ontario Housing Corporation thirty two years ago. The OHC budget currently finances rent-geared-to-income housing for a total of 125,000 households (84,000 OHC, 15,000 MTHCL, 23,000 rent supplement, and 3,000 rural and native housing units). This is 9% of the renter households in the province. What does this cost the taxpayer? In 1995 these 125,000 units cost \$632 per month – for everything, all subsidies and all operating and capital expenditures. Tenants paid \$276 per month (44% of the cost) and the provincial and federal governments split the other \$356 per unit per month. The total subsidy bill for 9% of Ontario's lowest income households was \$527 million. The Ontario share was \$257 million, which is about 0.5% of the provincial budget. For a 'non-ideal' bricks and mortar program, OHC's \$175 per unit per month cost is one of the best deals the Ontario government has ever financed. To replace OHC's units today would cost about \$5 billion.

What if no OHC, but a Shelter Allowance?

What if, in 1964, a shelter allowance program was established instead of OHC? OHC houses half families and half seniors. A conservative estimate of the existing average market rent for these households might be \$750 in 1995. These tenants can pay \$276 per month (their current rent-geared-to-income payments). An average \$474 per month shelter allowance would be required (\$5,688 per household per year). This would require a subsidy of \$711 million per year. Since the 60,000 households on the OHC waiting lists throughout the province would also qualify, this would be another \$341 million per year. Without addressing any of the other forms of housing need in the province, we would be spending more than a billion dollars a year. A properly funded shelter allowance program in Ontario would easily cost \$4 billion and might still have little impact on rental supply. Since we are not likely to see a new multi-billion dollar entitlement program of any type in Ontario, the debate over the cost and benefits of the shelter allowance option is a waste of time.

OHC's cost-effective investment over the past three decades demonstrates that government can (on occasion!) do things right. Given the passage of the same amount of time the investment in non-profit and co-op housing will show similar impressive financial results. In short, the combination of housing supply programs and rental sector regulations have not solved our housing problems, as the new Metro study documents. They have, however, been gradually addressing some of the social need for housing and offering forms of consumer protection given the long-standing market failure in the conventional rental housing supply sector. We need to continue this progress, not reverse it.

J.D. Hulchanski, University of Toronto
22 August 1996 Presentation to Ontario Legislature,
Standing Committee on General Government

APPENDIX #2

PRIVATE RENTAL SUPPLY THE BRITISH COLUMBIA 'EXPERIMENT'

July 2, 1996 memo to Al Leach, Minister

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July 2, 1996

To: Al Leach, Minister responsible for housing in Ontario
cc: Opposition housing critics in the Ontario Legislature

From: David Hulchanski, Professor, *Housing and Community Development*

Re: Private Rental Supply – The British Columbia ‘Experiment’
(or how to save money debating rent decontrol)

As I was looking through my research files on rent control I thought the attached four page excerpt from a study of British Columbia’s 1983 rent decontrol may help inform the debate.

The B.C. minister responsible for rent control in 1983 asserted that “*these deregulatory measures will ultimately result in new real estate development, more jobs and a continuing healthy availability of rental accommodation.*” He never defined “ultimately.”

A dozen years later “British Columbia is home to the lowest vacancy rates and some of the highest rents in Canada.” (*Rental Housing Trends in British Columbia*, BC Ministry of Housing, 1995, p.2.) There has been no supply response. Rents went up and there was no ‘down filtering’ because existing rental stock was either demolished or gentrified. A temporary glut of condo’s for rent, a continuing provincial social housing supply program, and increased numbers of often low quality apartments in houses are temporarily preventing a severe rental supply crisis in urban B.C.

There is no doubt that rent controls can distort and inhibit the functioning of *normal market* dynamics. The B.C. Social Credit government used this argument in the early 1980’s. They did everything they were advised to do according to the assumptions of conventional economic *theories*. The rental supply experiment failed because there were no *normal market* dynamics to distort or inhibit. The starting assumption for the policy change was simply wrong.

If private rental housing suppliers cannot meet ‘demand’ we have market failure. Normal functioning markets consist of supply and demand. There is very little *effective market demand* and a great deal of *social need* in urban rental markets. Social need is the portion of rental housing ‘demand’ the private market cannot respond to.

I have yet to see empirical evidence that unsubsidized private rental sector supply is or will be economically viable. The household income of most tenants is simply too low.

This lack of effective demand due to low-incomes among renters is worse now than it was when rent controls were introduced. The Metro Toronto government has just published a detailed study which documents the extent of the problem within greater Toronto (see, *Housing Patterns and Prospects in Metro*, June 1996). The real household income of renters has actually *declined* by 8% between 1971 and 1991 (while the income of owners has increased by 20%). Tenants had a median income of \$33,500 in 1991, which was \$30,500 *less* than homeowners (\$64,000). The market cannot build for households with such low incomes.

The saddest joke in debates over supply and demand is any mention of 'filtering.' The last twenty years have been a period of continuing 'up filtering' of the rental stock, that is gentrification and, prior to rental housing protection legislation in Ontario, conversion to ownership or other uses. 'Down filtering' has only occurred in U.S. cities. The end of the down filtering chain is the slum.

The few economists who still even mention filtering offer no empirical evidence. Long ago research identified the following problems with the filtering assumption: the inadequate volume of units available for filtering; the speed at which the few available units "trickle down"; the numerous breaks in the filtering chain; and the quality of the units which do filter down. In 1949 famed land economist Richard Ratcliff wrote: *The end product of filtering, at the bottom of the chain reaction, is substandard housing; thus filtering produces the very blight which we seek to remedy.*

I would hate to see past lessons ignored. I hope a realistic assessment of effective market demand and a more careful examination of the 'down filtering' assumption are carried out.

If the government is not planning to base its course of action on evidence and on the financial realities Ontario's renters face, may I suggest you at least save the taxpayer some money by using the attached as a script for the debate in the Legislature. There is no need to have staff prepare anything. You and the opposition members can read your respective parts from the transcript of the 1983-84 BC legislative debate. If we will not use research to learn from the past we can at least use it to save some money while we repeat the mistakes of the past.

Part of Chapter Three from:

C. Lazzarin, *Rent Control and Rent Decontrol in British Columbia: A Case Study of the Vancouver Rental Market, 1974 to 1989*,

Masters degree thesis, School of Community and Regional Planning,
University of British Columbia, April, 1990.

3.4 The Elimination of Rent Control in B.C.: 1983-84

Rent control was formally ended on 6 June 1983 with an announcement in the Finance Minister's annual budget. At the same time, the Social Credit government extended the rent review system (introduced in 1980) another year in an attempt to help smooth the transition to a rent control-free market. Rent regulation in British Columbia came to a complete halt in 1984 with the lifting of rent review. In 1984, a new Residential Tenancy Act was introduced which outlines the regulations that currently affect all residential tenancies.

In 1983, the NDP and the Social Credit Party once again differed over the question of how much government intervention in the rental market was required. The Social Credit Party eliminated rent control because of their long-held belief in the efficiency of an unrestrained market. Their confidence in the marketplace was made clear in the arguments put forward by Consumer and Corporate Affairs Minister Jim Hewitt. Referring to his government's elimination of rent control he said:

It's fair to say that this government identified this particular time as a window in which we could move to let the marketplace work and allow renters the opportunity to have available to them rental accommodation and have competition as opposed to government intervention in the marketplace. [1]

Mr. Hewitt went on to argue that fair rents should be determined by the rental market, not by government. In his words:

the competition of the marketplace will determine what price a person pays for an apartment. That's the way it should be. The marketplace should be allowed to work. [2]

He repeated the importance of an unfettered rental market in 1984 during the debate over the elimination of rent review. In his words:

Behind the thrust of this bill and many other pieces of legislation we've brought before this House is this key: the fact that government has been too involved in the marketplace in the past. [3]

Lands, Parks and Housing Minister Tony Brummet also viewed an unfettered private market as the best way to provide housing. In 1983, when asked about the effect that lifting controls would have on low-income earners, he said that "you have to have some faith in the market. Temporarily you may have a bit of a problem" for lower-income families he admitted "but I really think rents will come down to what people can afford." He predicted that in the long run, developers will begin to build cheaper apartments if that's all that people will rent. [4]

The Social Credit government argued that removing rent control would: a) result in increased rental construction; and b) result in higher vacancy rates. Landlords and tenants, they argued, would both be much better off. Speaking of these accrued benefits Jim Hewitt said that:

I believe these deregulatory measures will ultimately result in new real estate development, more jobs and a continuing healthy availability of rental accommodation. [5]

He went on to say that:

It is a renters' market. We move out of that field, and as time goes on new development will take place to fill the need for rental accommodation because landlords and developers are not bound by legislation as to what they can charge. As a result there will be a reasonable vacancy rate in the future as well as now. [6]

The Social Credit government also thought that lifting rent control would be a good character builder for the average British Columbian. In the words of Social Credit MLA Donald Campbell:

The people out there want to be able to provide for themselves. The people in B.C. are hard-working people, and they want to provide for themselves. But because the government has got involved in the marketplace so many times, it has destroyed the initiative of the people, so today they don't know what they should be doing. This government has to get out of the marketplace so that these people can provide for themselves. [7]

As in the earlier periods of rent control, the Social Credit Party substantiated their views by deferring to neo-classical economists. In 1983, Consumer and Corporate Affairs Minister Jim Hewitt said that removing rent control was the right thing to do because:

economists around the world state that rent controls are detrimental to the housing markets and to the consumer as well. [8]

During debate over the 1984 Residential Tenancy Act he again stressed his confidence in economists. In his words:

We feel, as economists have stated in the past and continue to state, that it will provide opportunities for new construction in a society where you don't have rent controls. [9]

The NDP were critical of the government's reliance on economists and economic institutions. Speaking on the 1983 budget that eliminated rent control, MLA Graham Lea said:

When you see the Fraser Institute and its director sitting in at the planning of the budget with the cabinet, and then you see everything that the Fraser Institute believes in coming into the Legislature in legislative form, you have to believe that there is some connection. [10]

The same criticism was raised by Robin Blencoe in 1984 during debate over the new Residential Tenancy Act:

what we have in British Columbia in terms of the Residential Tenancy Act and regulations...[is] not coming from some of the saner members of the government. It's coming from that weird and wonderful group, the Fraser Institute. They are the ones who are directing the government these days. [11]

The NDP's view of the rental market's inability to meet the needs of all British Columbians remained unchanged. They still maintained that the market possesses problematic flaws that prevent it from operating efficiently. Gary Lauk described the operation of the rental market this way:

To argue that the free market system will take care of rents ... You show me where one rent in the West End of the city of Vancouver has been reduced during the high vacancy rates. They don't go down in the free market system; they only go up ... The law of

supply and demand does not apply to accommodation. It doesn't work. Rents go up, they don't go down. [12]

Mr. Lauk repeated this argument in 1984 during the debate over the new Residential Tenancy Act. In his words:

there is no free enterprise in housing. There hasn't been in 7,000 years. There hasn't been free market housing in 7,000 years, and there never will be. There's no such thing as supply and demand in housing. It's always government-regulated or -effected control, directly or indirectly. You can't have it any other way. [13]

The NDP also argued that there was nothing new about government intervening in the marketplace. They maintained that rent control was just one of many forms of government intervention and that landlords and investors welcome government's involvement so long as it benefits them. In the words of Gary Lauk:

If you can't argue that rent controls are a form of artificial restraint in the free market system, then you'd have to argue that zoning is, that the control of interest rates in the central bank is and that the chartered bank act is. I find that the argument is a one-sided argument. Where a free market system benefits the owner, the investor, the industrialist or the banker, then he wants free enterprise. If it doesn't benefit him he wants regulation. [14]

The issue of landlord and tenant rights remained divisive at the time rent control was eliminated. The Social Credit government argued that it was time landlords had their rights, which were taken away under rent control, re-instated. In the words of Consumer and Corporate Affairs Minister Jim Hewitt:

We also recognized—which the NDP legislation would never really recognize—the fact that the landlord has rights. The landlord has some rights too, and certainly has the right to deal with his own property, in which he has made an investment, recognizing that he has to take into consideration the fact that a tenant occupies the premises. [15]

The NDP, on the other hand, viewed the termination of rent control as a regressive step in the advancement of tenant rights. NDP Housing Critic Robin Blencoe said that:

the government in its wisdom is going back or shifting the fine balance between landlord and property holders—or the landed gentry, if you will—in terms of their rights, and the idea that was starting to be built up in the province of British Columbia that tenants also had rights and that the equation should be fairly equal. However, there's a feeling in British Columbia that there's a philosophical shift by this government that tenants should have a minor position in that equation. [16]

Mr. Blencoe went on to call the proposed new Residential Tenancy Act “a landlords’ charter.” [17]

The NDP raised the issue of security of tenure again and argued that the elimination of rent control meant that tenants would not be protected from economic evictions. Robin Blencoe claimed that the proposed Residential Tenancy Act provided “tenants with weak tools with which to protect their security of tenure.” [18]

3.5 Summary

Rent regulation was clearly a hotly contested policy in British Columbia. There was no question in the minds of opposition members that it would create havoc not only with the housing market but with the investment mood and psychological well-being of British Columbians. The NDP were equally adamant that regulations were needed to combat inflation and to protect tenants from the rental market's shortcomings.

The positions of the NDP and the Social Credit Party remained consistent throughout the ten year period of rent regulation. The only exception is the 1975 provincial election when the Social Credit Party reversed their position and campaigned in support of rent control.

This chapter has shown that the basis of disagreement between the NDP and the Social Credit Party focused primarily on two issues: a) the confidence that each party placed in the private market; and b) the balance of rights between landlords and tenants. The NDP believed that the private market did not always provide for social justice and that such instances justified government intervention. They also maintained that tenants needed more rights to equal the balance between themselves and landlords.

Furthering social justice was not the Social Credit Party's frame of reference for this issue. Their concern focused on the ability of the market to operate efficiently with a minimum of government intervention. With respect to the issue of landlord-tenant rights, they believed that rent control unfairly increased tenant rights at the expense of a properly functioning rental market. They believed a properly functioning rental market would protect tenant rights better than a government regulated rental market.

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1. Jim Hewitt speaking on the 1983 Residential Tenancy Act. Debates of the B.C. Legislative Assembly, 10 August 1983, p. 727.
 2. Jim Hewitt discussing Bill 5, British Columbia Legislative Debates. 12 July 1983, p. 248.
 3. Jim Hewitt speaking on the 1984 Residential Tenancy Act. Debates of the B.C. Legislative Assembly, 10 April 1984, p. 4321.
 4. The Vancouver Sun, 15 September 1983, p. A3.
 5. Jim Hewitt discussing Estimates: Ministry of Consumer and Corporate Affairs. B.C. Legislative Debates, 19 October 1983, p. 2849.
 6. Ibid. p. 2855.
 7. Donald Campbell speaking on Bill 5. Debates of the B.C. Legislative Assembly, 18 August 1983, p. 908.
 8. Jim Hewitt speaking on the 1983 budget debate. Debates of the B.C. Legislative Assembly, 12 July 1983, p. 248.
 9. Jim Hewitt speaking on Bill 19, the proposed 1984 Residential Tenancy Act. Debates of the B.C. Legislative Assembly, 10 April 1984, p. 4320.
 10. Graham Lea speaking on the 1983 budget that ended rent control. Debates of the B.C. Legislative Assembly, 23 September 1983, p. 1916.
 11. Robin Blencoe speaking on the 1984 Residential Tenancy Act 9 April 1984, p. 4308.
 12. Gary Lauk, discussion over Bill 5. B.C. Legislative Debates, 12 July 1983, p. 220.
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 14. Gary Lauk (NDP) speaking on Bill 5, Debates of the Legislative Assembly (British Columbia) 19 October 1983, p. 2856-57.
 15. Jim Hewitt speaking on Bill 19 (1984 Residential Tenancy Act). Debates of the B.C. Legislative Assembly, 10 April 1984, p. 4320.
 16. Robin Blencoe speaking on the Residential Tenancy Act (Bill 5). Debates of the B.C. Legislative Assembly, 20 October 1983, p. 2882.
 17. The Times-Colonist 5 April 1984, p. B1.
 18. The Victoria Times-Colonist 4 May 1984, p. A4.

J.D. Hulchanski, University of Toronto
22 August 1996 Presentation to Ontario Legislature,
Standing Committee on General Government

APPENDIX #3

THE IMPACT OF REMOVING RENT CONTROLS IN B.C., 1983

From
Rental Housing Trends in the City of Vancouver,
by J.D. Hulchanski, UBC Centre for Human Settlements,
Research Bulletin, April 1989.

4. The Supply of New Private Rental Units

What are the prospects for future supply of unsubsidized private sector rental units? Not very good.

MURB, ARP and CRSP

Since the early 1970's, most private sector rental starts have been subsidized. Over the recent decade, most were also registered as condominiums to avoid municipal condominium conversion regulations. The rental units subsidized by the MURB program, the Assisted Rental Program (ARP) and the Canada Rental Supply Program (CRSP) will only be in the rental sector for a short period. The length of time depends on program regulations, local housing market conditions, and the investment strategies of the owners.

Between 1975 and 1985 the MURB, ARP and CRSP programs subsidized 23,200 rental units in the Lower Mainland. About 19,200 of these units were subsidized by the MURB and ARP program and 4,000 by the CRSP program. About 85 percent of these units were registered as condominiums at the

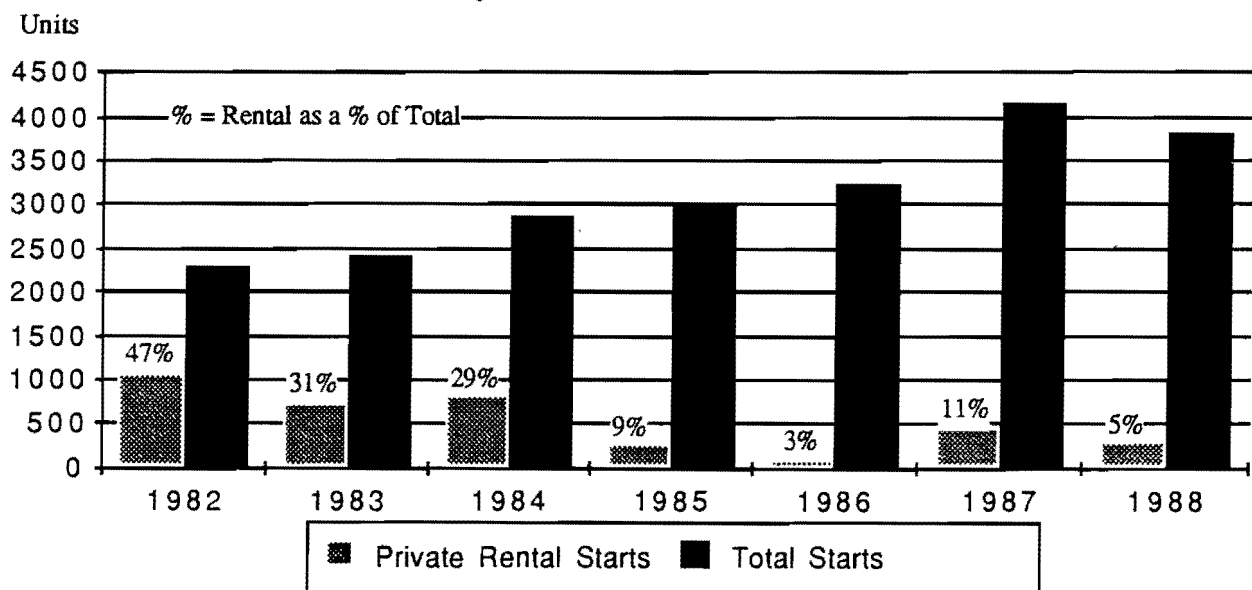
time of construction. The City of Vancouver's share of these units is: 6,790 MURB/ARP units (35% of the Vancouver region total) and 1,027 CRSP units (26% of the total CRSP units built in the region). It is the MURB rental projects which are now being lost to condominium conversion in large numbers. ARP and CRSP project owners are able to buy their way out of their CMHC commitments in order to convert.

5. The Impact of Removing Rent Controls in 1983

The federal rental supply programs were designed on the assumption that the private rental market was basically sound and that it only required temporary subsidies to help get things going.

Rent controls, in particular, were blamed for being the cause of most, if not all, of the problems of the private rental sector. Get rid of these market interferences, the theory went, and "market equilibrium" would return. The supply of rental units would begin to meet the demand. Even social housing supply programs, some argued, could be curtailed

Private Rental Starts and Total Starts
City of Vancouver, 1982 to 1988



Source: CMHC Vancouver Branch

because they were considered "unfair competition" by some condominium developers and, in any case, it was argued, the private sector is more efficient than non-profit and co-op housing developers.

Based on this theory, Vancouver's rental sector should be fine by now. Rent controls were abolished in 1983. Demand remained high, even during the recession. The market failed to respond with new supply, even after the recession ended and demand was even higher. The only measurable impact of the removal of rent controls was sharp increases in rents once the recession was over. There has been no positive supply impact.

The Problem -- Supply, Not Demand

The problem is not a lack of demand -- there is plenty of demand for rental units. It is the lack of *effective* market demand: tenants simply cannot or will not pay the rents required to make private supply of rental stock economical. Once rent levels approach the monthly mortgage costs of a modest condominium or house, tenants with enough of a down payment have every incentive to choose the ownership option. Lower income renters have no choice *and* cannot pay higher rents.

Renters have lower median income levels than owners and more renters have incomes near or below the poverty line. Rather than effective market demand, lower income renters create social need which the market cannot respond to. Supply of housing affordable to renter households, therefore, is the problem. Loss of existing affordable rental stock only adds to the problem.

Furthermore, the high and rapid economic return produced by condominium development competes with potential rental projects. Condominium investors are always able to pay more for building sites than rental investors because condominium buyers can pay and are willing to pay more than renters.

Market Failure in the Private Rental Sector

In sum, there is very little reason for believing or hoping that unsubsidized private sector supply of rental units will be viable again. There is market failure in the private rental sector. Any theories or arguments about rental policies based on the

assumption that Vancouver's rental sector is viable as a properly functioning market are simply wrong.

Rent controls, for example, are opposed by some on the basis that they distort and inhibit the functioning of market dynamics. There are no normal market dynamics to distort or inhibit any longer. The B.C. government bought this argument in the early 1980's and did everything they were supposed to do to restore the private rental sector. The experiment has lasted more than five years and has failed.

Four Rationales For Rent Regulations

Under conditions of market failure there are four rationales for rent regulations.

1) ***Security of Tenure:*** Where the rental market is not functioning normally, where vacancy rates and new rental supply are at low levels, rent regulations protect consumers who find themselves in an inferior bargaining position with their landlord.

2) ***Maintenance of the Affordability of the Existing Rental Stock:*** Rent regulations decrease the occurrence of sudden, abnormal, and "unfair" rent increases in times of limited vacancies, in times of general inflationary pressures, and in times of extreme speculative pressures in the land and housing markets. The aim is to prevent the existing stock from becoming increasingly unaffordable.

3) ***Prevention of Regressive Income Redistribution:*** If rents were allowed to rise simply because the market is unable to function normally, the owners of rental accommodation would benefit from their unique market position as owners of a scarce commodity that is not only in high demand but also a basic necessity. Rent regulations prevent or minimize the redistribution of income from tenants to owners of rental accommodation.

4) ***Mediation of Conflicts Relating to Rental Tenure:*** The most fundamental element of the landlord and tenant relationship is the rent itself. Rent regulations, not simply landlord and tenant legislation, establishes a more balanced power relationship. Only through rent regulations is the most important issue in the landlord and tenant relationship, changes in rents, negotiable before a public commission via established rules and procedures.

5. *Where to Next? Define Policy Options*

Is the City willing to take measures to ensure that there is a private rental sector in the future? Should renter households continue to be pushed out of the City or into crowded or inadequate accommodation in order to allow condominium conversions and demolitions to take their "natural" course? Three of the four major segments of the City's rental stock are threatened: the purpose-built rental apartments; the secondary suites in some neighbourhoods; and the rooming house stock in and near the Downtown Eastside neighbourhood.

This brief review of rental trends has pointed out that the private rental market has failed to function, that thousands of good rental units are being lost each year, and that there is a demand for rental housing that is not being addressed. Much of the newest private sector "rental" stock built under government programs between 1975 and 1984 is at risk. The total number of the purpose-built apartment and townhouse rental units are in rapid decline. This sector is not sustainable unless immediate regulatory action is taken.

The next largest segment of the rental stock is highly successful and dynamic yet it is "illegal." Secondary suites now account for more than twenty percent of the rental stock -- produced with no help from any level of government. A portion of this stock is inadequate and rehabilitation assistance may be appropriate in combination with building code enforcement.

The next largest part of the rental sector is social housing. Much of this stock is secure. It is a permanent part of Vancouver's affordable rental stock. Yet fewer and fewer new units are being added to this sector each year.

A characteristic of the secondary suites and much of the social housing stock is that both are the result of small scale initiatives -- either private or group-sponsored -- which lead to incremental gains in secure or reasonably secure affordable rental stock. These are the only parts of the City's rental stock which are increasing. This kind of household and community-based activity must be encouraged and supported.

Once a clearer understanding of what is happening to the City's rental stock becomes more widespread, it will be possible to begin to map out an overall strategy. What kind of actions at municipal, provincial and federal levels are required to protect, maintain and improve the quality and the quantity of the housing in each part of Vancouver's rental sector? As a first step, however, the rapid loss of the existing purpose-built rental stock must be stopped or there will be very little to protect, maintain and improve.

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J.D. Hulchanski, University of Toronto
22 August 1996 Presentation to Ontario Legislature,
Standing Committee on General Government

APPENDIX #4

THE FILTERING PROCESS

From
Market Imperfections and the Role of Rent Regulations,
by J.D. Hulchanski, Commission of Inquiry into
Residential Tenancies, Research Study No. 6, 1984.

Market Imperfections and the Role of Rent Regulations in the Residential Rental Market

by J. David Hulchanski

Commission of Inquiry into Residential Tenancies, Research Study No. 6

Government of Ontario, Toronto

December 1984 [ISBN - 0-7743-9916-3]

from Chapter 3.2, section on "Problematic Characteristics of Housing as a Market Commodity"

The Filtering Process.

It is generally recognized that the private market supply mechanism cannot meet the demand for housing of lower-income households by direct construction of the required units. Very little, if any, of this demand can be met by new construction because the market cannot build units that lower-income households can afford unless government provides fairly significant subsidies. In the current rental market, for example, the development industry's estimate is that the value of the subsidies required to produce even MURB and CRSP units, which generally rent at the upper end of the market, needs to be in the range of 25 to 30 per cent of total capital costs (Canadian Institute of Public Real Estate Companies 1982, 3).

The fact that the private market cannot provide rental units for lower- or even moderate-income households has not been defined as a market failure by conventional theorists, who assume that by an indirect process known as "filtering" the market mechanism can effectively meet this demand. Filtering would, in theory, generate a backward chain of movements when new units are built. As the new units are occupied, whole groups of households move upward and the housing situation in general improves. Thus an increase in the housing stock at the upper end of the housing spectrum is supposed to be beneficial to all households. In

fact, there appears to be a wide gap here between theory and reality. British and American analysts have identified the four problems with the efficiency and equity of the filtering process.

First, an inadequate volume of units is being made available to the filtering process. There are many more lower-income households than higher income households. Yet, the market responds best, and often only, to demand in the higher income groups. As Boddy and Gray point out,

One may question the volume of housing available to filter down to lower-income households. Since the distribution of household incomes tends towards a pyramidal shape, building new houses for those high up the pyramid will simply not release enough houses for those further down where the pyramid is wider. There are too few high-price and high-quality houses to meet the needs of lower-income households. (1979, 46)

It is unlikely that a rational development industry would overbuild at one end of the market, since the over-supply would only depress market prices.

The second problem is speed: to the extent that filtering takes place, how quickly do units actually filter down? Collard notes that filtering is, at best, a slow and protracted process:

One could not expect rapid results from such a programme as the filtering process could be quite a protracted one, especially if there was already overcrowding in medium to poor type rented accommodation. The easing of the situation at the top of the housing scale would be blocked and therefore fail to trickle down to the really deprived groups. (1972, 171)

Thus the market mechanism could not, through the filtering process, meet an increase in demand among lower-income households very quickly.

Not only does filtering take time, but the units can get displaced on the way. The third problem with filtering is that breaks in the filtering chain can prevent whatever units may be available from reaching the lower strata of the marketplace. New households are continually entering the market to take up some of the supply, but in recent years this factor has been a less significant obstacle to filtering than the combination of demolitions, conversions, and gentrification. Many things can happen to a housing unit. In very tight markets, filtering is one of the least likely. According to Lansley,

the main weakness of the filtering process is that... many of the vacancy chains are broken before the poor benefit to any significant degree. We have already seen that new building only adds 1 to 2 per cent at the most to the stock each year and there is evidence that such new private building has its greatest impact in improving the space occupied by the better-off and that little of the benefit is passed on to less affluent groups. Moreover, unmitigated, this process would simply lead to the permanent concentration of poorer households in the lowest quality housing and thus has indefensible distributional consequences. (1979, 25-26)

The fourth problem with the filtering assumption is that the units that do eventually filter down are often of poor quality, a circumstance that leads to the inequitable distributional consequences that Lansley refers to above. It is unlikely that the quality of a unit will remain the same, let alone increase, as it filters down. Serious deterioration in the condition of

the unit is much more likely. The entire history of low-income households' living in unfit and substandard units demonstrates the shortcomings of the filtering assumption. Where filtering does take place, and it certainly has taken place in the history of many European and American industrial cities, the result is often the classic slum neighbourhood. It is not only the housing unit but the surrounding neighbourhood that must filter down before lower-income households can afford housing units on the private market. This is a process that R.U. Ratcliff described decades ago in his book *Urban Land Economics*:

The end product of filtering, at the bottom of the chain reaction, is substandard housing; thus filtering produces the very blight which we seek to remedy. (1949; quoted in Boddy and Gray 1979, 47)

It is difficult, therefore, to assume that the market will supply units to lower-income households through the filtering process. There are no empirical studies of filtering in Canada, but the conceptual problems are sufficient to cast doubt on its effectiveness. Boddy and Gray conclude their study of filtering with a sobering indictment:

The concept of filtering is derived from a laissez-faire, market economy view of how the housing system operates -- or how it should -- and has in turn been used to support and legitimate this viewpoint in terms of public policy. The persistence of inadequate housing and of high status residential areas in the USA and UK, and the contradictory processes of "gentrification" and disinvestment by landlord and low income owners indicate the empirical bankruptcy of filtering as a general description of the housing system. The numerical insignificance of high quality dwellings, the effects of racial discrimination in the USA, and subsidies such as tax relief on mortgage interest and untaxed capital gains for home-owners in the UK all contradict the assumptions of the theory. The concept is theoretically unsound and hence of only limited empirical validity. (Ibid., 50)